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IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1967.

No. 471

T. B. PEELER and MRS. T. B. PEELER,
Petitioners,

v.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI

To the United States Circuit Court of Appeals for the Fifth Circuit.

J. RENE HAWKINS,
P. O. Box 4348,
Macon, Georgia 31208,
Counsel for Petitioners.

ST. LOUIS LAW PRINTING CO., INC., 411-15 N. Eighth St., 63101. CEntral 1-4477.

INDEX.

	Page
Opinions Below	1
Jurisdiction	2
Questions Presented	2
Statutes Involved	3
Statement	4
Reasons for Granting the Writ	6
Conclusion	11
Appendix A	13
Appendix B	17

CITATIONS.

Cases:

Albritton v. Commissioner, 248 F. 2d 49	9
Barker v. Commissioner, 250 F. 2d 195 (2 Cir. 1957)	8
Burnet v. Harmel, 287 U. S. 103, 53 S. Ct. 74	9
Crowell Land & Min. Corp. v. Commissioner, 242 F. 2d 864	9
Robert M. Dann, 30 T. C. 499	8
Gowans v. Commissioner, 246 F. 2d 448; C. C. A. 9 1957 citing Commissioner v. Southwest Exploration Co., 350 U. S. 308, 76 S. Ct. 395	8
Hodges v. Georgia Kaolin Co., 108 Ga. App. 115, 132 S. E. 2d 86	7, 10
Laudenslager v. Commissioner, 305 F. 2d 686, 690-91, Cert. denied 371 U. S. 947, 83 S. Ct. 501	8

Linehan v. Commissioner, 297 F. 2d 276 (1 Cir. 1961) 6, 8, 9
Turner v. United States, 226 F. Supp. 970, 13 AFTR 2d 899 8

Statutes:

Internal Revenue Code of 1954—
Sec. 61 (26 U. S. C. A. 61) 3
Sec. 611 (26 U. S. C. A. 611) 3
Sec. 1221 (26 U. S. C. A. 1221) 3

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To the United States Circuit Court of Appeals for the Fifth Circuit.

Petitioner Prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit, entered in the above entitled case on May 11, 1967.

OPINIONS BELOW.

The opinion of the District Court (R. 34) is reported at 238 F. Supp. 640. The opinion of the Court of Appeals in this case (R. 44) is printed in Appendix B hereto, p. 17. The opinion of the Court of Appeals in a compan-

ion case, reference to the opinion of which is material to a full understanding of the Circuit Court's opinion in this case, is Case Number 22,693 of the Fifth Circuit Court of Appeals, **Wood v. United States,** decided May 11, 1967 (R. 49), printed in Appendix B hereto, beginning at page 21.

JURISDICTION.

The judgment of the Court of Appeals was entered on May 11, 1967 (Appendix B, p. 17, infra). The jurisdiction of this court is invoked under 28 USC, Sec. 1254 (1).

QUESTIONS PRESENTED.

Whether the proceeds received under an agreement for the removal of crushed stone constitute proceeds from the sale of all of a mineral in place, thus being proceeds from the sale of a capital asset; or whether taxpayer retained an economic interest in the minerals so as to render such proceeds "royalties", and taxable as ordinary income.

STATUTES INVOLVED.

Internal Revenue Code of 1954—

Section 61,
Section 611, and
Section 1221.

Each of these statutes is printed in the Appendix A hereto, beginning at p. 13.

STATEMENT.

Taxpayers, husband and wife, filed a joint return for the years 1957, 1958, and 1959, reporting the proceeds from an arrangement with Weston & Brooker Company, a stone quarrying company, as gain from the sale of a capital asset. The Internal Revenue Service determined that the taxpayers had erroneously reported such receipts on the basis that the proceeds were royalties and as such should be taxed as ordinary income. A deficiency was accordingly assessed for these years.

Taxpayers paid these deficiencies, filed timely claims for refund which were disallowed, and in due course, filed suit under Title 28, USCA, Sec. 1346 (a) (1), in the District Court for the Middle District of Georgia.

Based upon the pleadings and an affidavit of taxpayer, T. B. Peeler, the Petitioners filed a motion for Summary Judgment on the ground that there was no genuine issue as to any material fact and that they were entitled to judgment. To this the Government filed a cross-motion for Summary Judgment on the grounds that there was no dispute as to a material fact and based on such undisputed facts, the Government was entitled to a judgment as a matter of law.

Taxpayer petitioner owned a tract of 219 acres of land in Jones County, Georgia. The Weston & Brooker Company of Columbia, South Carolina, wished to prospect for stone on this tract of land to determine if there was a sufficient deposit to justify its carrying on a mining and quarrying operation.

Accordingly, on May 5, 1955, an agreement (R. 26) was entered into between the taxpayer and the mining company with regard to the purchase of stone. This agreement had a two-fold purpose. First, to give the company

the right to prospect for stone, and secondly, if stone was found, the right to purchase the stone at a price designated in the agreement. The agreement referred to the parties as "Lessor" and "Lessee", and the purchase price was referred to as "royalties". The arrangement under this agreement was to last for twenty years. "Royalties" were to be 3¢ per ton of 2000£ and 2¢ per ton of 2000£ sand shipped.

After making a determination that there was a sufficient stone deposit to conduct a mining operation, an officer of the mining company approached the taxpayer and expressed a desire to obtain an amendment to the original agreement so as to convert the twenty-year agreement into an agreement extending for an indefinite period beyond the original twenty-year agreement, so that there would be sufficient time to remove the entire deposit of stone. Such an amendment was made (R. 31).

The mining company, thereupon, entered the premises, stripped the over-burden from said land of some fifteen to twenty-five feet in depth, and removed all standing trees, timber and vegetation so as to be able to quarry the stone on said property.

There is upon the property a pit from which stone has been removed to a depth of 110 feet and extending over fifty to sixty acres. The company intends to mine the entire stone deposit, which according to their estimate covers the entire 219 acres to a depth of 600 feet. It is noted that at the present rate of extraction, it will take the mining company more than 150 years to complete this operation. Therefore, in the end, all that will be left for the taxpayer's heirs is a useless hole 600 feet deep extending over 219 acres.

The company considers this a permanent operation and it is estimated that the mine operator has expended the

sum of $1,750,000 in the purchase and installation of quarrying and mining machinery and equipment.

Payments to the taxpayer are made monthly on the quantity of crushed stone shipped from the quarry.

The District Court found that the taxpayer, in fact, if not in form, sold the entire mineral deposit to Western & Brooker, that the taxpayer retained no economic interest in such deposit, and that the proceeds from the transaction are entitled to capital gain treatment.

Accordingly, the District Court granted the taxpayer's motion for Summary Judgment and denied the motion filed by the Government.

On appeal by the Government, the United States Court of Appeals for the Fifth Circuit reversed the judgment of the District Court, basing its reasoning primarily on that expressed the same day in the opinion rendered by it in **Wood v. United States**, No. 22693 (19 AFTR 2d 1435).

REASONS FOR GRANTING THE WRIT.

I. The decision of the United States Court of Appeals in the instant case and in **Wood v. United States** (Appendix B infra), the authority upon which the instant case was decided, are directly in conflict with the decision of the First Circuit Court of Appeals in **Linehan v. Commissioner**, 297 F. 2d 276.

The Circuit Court, in the instant case, attempted to draw a factual distinction between the **Wood** case, supra, and **Linehan**. Such a distinction is invalid.

Such a distinction is invalid particularly with reference to the instant case, Peeler. By trying to distinguish the **Linehan** case from the Wood case, the Circuit Court draws out certain facts which indeed make Linehan indistin-

guishable from Peeler, e. g., "In Linehan the gravel company was obligated to remove all of the sand and gravel down to a specific grade", **Wood**, supra (Appendix B, infra).

In the instant case the miner, due to local law, was under an implied obligation to mine the stone, presumably to exhaustion, under the prevailing Georgia Law (**Hodges v. Ga. Kaolin Co.**, 108 Ga. App. 111).

In addition to the implied obligation under law, the conduct of the petitioner and the mining company indicates that all the mineral is to be removed.

A survey was made which indicated that the rock went to a depth of 600 feet over the entire 219 acres.

The parties re-negotiated the original agreement so that the miner would be certain that he would have sufficient time to remove the entire mineral deposit.

The miner moved onto the property extensive and expensive mining machinery and equipment, took complete charge of the entire tract, and gave every evidence that he intended to make a permanent installation.

The agreement pertained to only certain types of minerals and specific excluded others (R. 30).

The agreement related to a specifically defined 219 acre area and the mineral deposit according to the best information available was located on the entire area to a depth of 600 feet.

The mine operator cut the timber and stripped the overburden upon a substantial portion of the tract and began an operation which has been in effect for approximately ten years.

Upon completion of the mining operation, all that will be left is a dangerously large hole.

The Fifth Circuit Court itself, in **Wood** in Footnote 22 (Appendix B, p. 36), acknowledges that it is in conflict with the decision of the First Circuit in Linehan:

> "This is not to imply that presented with the factual situation before the court in Linehan, we would reach the same result."

The conflict is clearly shown by the fact that Peeler is so factually close to **Linehan** as to be indistinguishable and the Fifth Circuit has, in light of the similarity, held that Peeler retained an economic interest in the minerals contrary to the decision that would have been rendered in the First Circuit.

Furthermore, the Fifth Circuit cites **Laudenslager v. Commissioner** (2 Cir.), 1962, 305 F. 2d 686, as supporting their decision in the **Wood** case, supra, and Laudenslager and Linehan are acknowledged to be in irreconcible conflict with each other (**Turner v. U. S.**, 226 F. Supp. 970; **Laudenslager**, supra, footnote 4, p. 692).

The similarity of the obligation to mine in **Linehan** and **Peeler** puts a flavor on the facts in the **Peeler** case different from the **Wood** case, so that the rule regarding "economic interest" in **Barker v. Commissioner**, 2 Cir. 1957, 252 F. 2d 195 and **Gowans v. Commissioner**, 9 Cir., 246 F. 2d 448, should be applied to the facts in Peeler. In addition, the Peeler case is factually similar to the Tax Court case of **Robert M. Dann**, 30 T. C. 499, which conflicts with the Wood decision.

Also, the undisputed facts in the case at hand show, as the District Court below found, that in fact, if not in form, the taxpayer sold the entire mineral deposit (R. 37).

II. The Court of Appeals has decided an important question of federal tax law which the Supreme Court of the United States has not previously passed upon, but which should be decided by this Court.

A. The Supreme Court has previously passed upon the definition of an "economic interest" in oil and gas cases for purposes of determining entitlement to depletion allowance **but has never ruled** upon the question of "the sale of all minerals in place" or "the retention of an economic interest" insofar as the same applies to cases involving hard minerals. (**Burnet v. Harmel**, 1932, 287 U. S. 103, 53 S. Ct. 74, 77 L. Ed. 199 (relates to oil and gas)).

B. The Circuit Courts have created confusion for the taxpayer in determining how transactions relating to the sale of hard minerals must be reported for federal income tax purposes.

The Court will take notice that in the affairs of men it is perilous to a buyer's financial position for such buyer to purchase for a lump sum all of a given mineral substance to be found on a specific tract of land. It does not change the character of a sale when the price for the mineral has to be determined by measure to be taken after the agreement has been made as in **Crowell Land & Min. Corp. v. C. I. R.**, 242 F. 2d 864.

The question always to be determined in these cases is whether the owner has retained an economic interest in the deposits. (**Laudenslager**, supra.)

While the words used by the parties in designating their relationship cannot be ignored, it is well established that we must look to the substance of the transaction to determine the essential character. (**Linehan**, supra; **Albritton v. C. I. R.**, 248 F. 2d 49 (5 Cir.).)

The Circuit Court has glossed over the facts and circumstances appearing in the record of the **Peeler** case and simply relegated the parties to the labels by which they call themselves. There are ample facts in the District Court record to justify and even compel a ruling that

the parties in fact, if not in form, intended a sale of all of the mineral in place (R. 37).

The Circuit Court states in its opinion in the Peeler case (R. 44) in commenting on **Hodges v. Georgia Kaolin Co.**, supra, that such decision by the Georgia Court merely "requires a miner who has cut timber and removed over-burden to make a reasonable effort to render the mining operation profitable . . ."

A careful reading of the case will surely indicate that the holding of the Court is best set forth in headnote (1) of the opinion:

> "(b) Where the lessee notifies the lessor to remove the timber from the land and then proceeds **itself** to remove the over-burden on a substantial portion thereof, the obligation immediately arises on its part under the provisions of the lease to **proceed with reasonable diligence in a mining operation**" (Emphasis supplied).

Indeed, a further quotation from the **Hodges** case, supra; in the Georgia Courts' decision on Motion for Rehearing, seems to bear out this Petitioner's interpretation of the impact of **Hodges** upon the question here under consideration:

> ". . . He (lessee) simply insists that the lessee, having notice of its intention to begin the mining and having taken steps in preparing the land for mining, which the lease provides may be done for that purpose, and thus having rendered a substantial portion of his land unfit for other purposes; may not thereafter sit idly by and allow the land to remain undeveloped or unmined."

Further, the contract in the Hodges case, supra, by its terms also provided for voluntary termination as did the contract in the Peeler case.

CONCLUSION.

For the reasons stated herein the Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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J. RENE HAWKINS,
Counsel for Petitioners.